



STATE BOARD OF EQUALIZATION STAFF LEGISLATIVE BILL ANALYSIS

Date Introduced:	02/19/02	Bill No:	SB 1501
Tax:	Sales and Use	Author:	Johnson
Board Position:		Related Bills:	SB 1502 (Johnson)

BILL SUMMARY

This bill would require the Board to exhaust all available collection remedies against a seller of a business or stock of goods who is liable for amounts due to the Board before pursuing collection efforts for that liability against the successor. The bill would additionally relieve the successor of any interest and penalty on the liability that accrued prior to the Board exhausting those remedies.

ANALYSIS

Current Law

Under existing Section 6811 of the Sales and Use Tax Law, if any person who is liable for any amount of tax sells out his or her business or stock of goods or quits the business, his or her successors must withhold from the purchase price an amount sufficient to cover that liability until the seller produces a receipt from the Board showing that the liability has been paid or a certificate stating that no amount is due. Section 6812 requires that if this procedure is not followed, the successor (purchaser) becomes personally liable for the seller's liability, to the extent of the purchase price of the business. The Board is required to notify the successor of the liability no later than three years after the Board is notified of the purchase of the business or stock of goods.

Section 6814 allows the Board to relieve a successor of any accrued penalties if the failure to withhold a sufficient amount of the purchase price is due to reasonable causes and circumstances beyond the successor's control. Current law does not allow the Board to relieve the accrued interest.

Proposed Law

This bill would amend Section 6814 of the Sales and Use Tax Law to require the Board to exhaust all available remedies, legal and administrative, to collect any amount due under the Sales and Use Tax Law from the seller of the business or stock in trade under a contract prior to enforcing the obligation against the successor. The bill would further provide that the successor is relieved of any penalty and interest on the obligation until the Board has exhausted its remedies against the seller.

The bill would become effective January 1, 2003.

This staff analysis is provided to address various administrative, cost, revenue and policy issues; it is not to be construed to reflect or suggest the Board's formal position.

In General

Any purchaser who fails to obtain the necessary tax clearance from the Board, or who fails to withhold the predecessor's liability from the purchase price of the business, becomes liable as of the date of the purchase of the business or as of the date the predecessor's liability becomes final. As a policy, first efforts to collect the amounts owed are directed against the predecessor. This policy is adhered to as long as collection in full can be made within a reasonable period of time, either directly from the predecessor or from assets belonging to the predecessor held by a third person. However, this policy is disregarded if collection from the successor will become jeopardized by delaying future collection action.

A "Notice of Successor's Liability" billing may be issued under the law not later than three years after the Board is notified in writing of the purchase of the business or stock of goods. The statute of limitations for issuance of the notice does not begin to run until the Board has been notified in writing of the purchase of the business. If there is no notification, *there is no statute of limitations*.

On average, the Board issues approximately 80 to 90 billings for successor liability each year.

Background

The provisions that allow for a successor of a business or stock of goods to be held personally liable for the former owner's liability have been in the Sales and Use Tax Law since 1943. Recognizing that successors are often caught unaware of the liability until after the Board mails its notice of liability, the Board has sponsored provisions in the past to "soften" the statute. For example, in 1979, through the enactment of SB 287 (Ch. 260), the Board sponsored amendments to Section 6814 to give a successor a statutory procedural remedy for contesting a liability asserted against him for the seller's sales and use tax obligations. Prior to enactment of SB 287, a successor was given some kind of opportunity to contest the liability, however, there was no statutory right to do so and the procedure was not uniform. The remedy in SB 287 is essentially equivalent to that of petitioning an ordinary determination of a sales or use tax liability.

In 1989, the Board also sponsored SB 151 (Ch. 768) to amend Section 6814 to establish a statute of limitations concerning notices of successor liability, and to establish the authority to relieve penalties originally imposed upon the seller of the business that are included in the successor billings. Prior to enactment of this measure, the successor had no opportunity for relief of any penalties incurred by the seller that were included within the liability assessed against the successor. Also, there was no provision in law to require the Board to mail the notice of successor liability within a specified time period. This measure required the Board to mail the notice within three years from the date the Board is notified of the purchase of the business.

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COMMENTS

1. **Sponsor and purpose.** This bill is sponsored by the author. Its purpose is to require the Board to pursue all collection efforts against the seller of the business prior to pursuing collection efforts against the successor, and to relieve the successor of the penalty and interest that accrued until the Board has exhausted its remedies against the seller. In a specific case brought to the author's attention, the Board issued a notice to a successor of a liability incurred by the predecessor of the business. The notice was mailed years after the business was purchased, and by that time, had a significant amount of accrued interest. The successor tracked down the predecessor who had moved to Texas and notified the Board, but the Board continued seeking collection efforts solely from the successor.
2. **The bill should specify to what extent available collection remedies should be exhausted.** The Board has a number of collection remedies it utilizes to collect delinquent amounts owed. At the administrative level, for example, on the day a tax becomes due and payable but remains unpaid, a state tax lien is created for the amount owed. The lien is in force for ten years and may be extended by re-recording the lien with any county or with the Secretary of State within the ten-year period. With respect to a state tax lien that can be in force for 10 years or more, at what point would the Board's remedies be exhausted under the provisions of this measure?
3. **Should the provisions of this bill apply to incorporations and other changes of ownership between related entities?** While a successor to a business is often an unrelated party, successor liabilities can also arise from situations in which a sole proprietorship incorporates, or where a partner takes over a business. Perhaps the author may wish to limit the provisions of this measure to purchasers of businesses unrelated to the sellers.
4. **Technical amendments.** Since the bill would provide the successor with automatic relief of accumulated interest and penalties incurred by the predecessor, the existing relief of penalty provisions contained in subdivision (b) should be stricken from the bill. Also, on line 26, the apostrophe should be deleted from the word "it's."
5. **Related legislation.** A similar measure to provide relief of penalty and interest for a successor has also been introduced by Senator Johnson (SB 1502). That measure would provide relief of the interest and penalty that has accrued prior to the successor being notified of the liability of the predecessor.

COST ESTIMATE

Administrative costs would include additional staff time devoted to collection efforts against the sellers, revising Board manuals, and providing directives to staff. These costs are expected to be absorbable.

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REVENUE ESTIMATE**Background, Methodology, and Assumptions**

During calendar year 2001, the Board issued 78 successor liability billings. The amount of penalty and interest that had accrued prior to the notification of the successor's liability amounted to \$2.9 million. The amount of the tax liability on these billings amounted to \$3.9 million. At the current 10% rate of interest on underpayments, an additional \$390,000 in interest would accrue for each year that the notification is delayed.

Revenue Summary

The revenue loss from relieving the successor of any interest and penalty that has accrued prior to a specified notice is estimated to be \$2.9 million annually. An additional \$390,000 in interest would accrue for each year the notification of the successor's liability is delayed. This revenue loss would be reduced to the extent that the Board is able to collect this interest and penalty from the predecessor prior to beginning collection activities against the successor.

Analysis prepared by:	Sheila T. Sarem	445-6579	03/15/02
Revenue estimate by:	Dave Hayes	445-0840	
Contact:	Margaret S. Shedd	322-2376	

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